National Tea Co.
Annual Report 1973

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Chairman, Loblaw Companies Limited

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Executive Officer

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Vice President, Finance
and Secretary Treasurer

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Barrister and Solicitor

W. Struan Robertson, Q.C.
Partner, Borden, Elliot, Kelley
& Palmer Attorney

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Chairman of the Board
George Weston Limited

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Executive Officer

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Vice President, Finance
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Vice President, Personnel

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Vice President, Real Estate
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Comptroller

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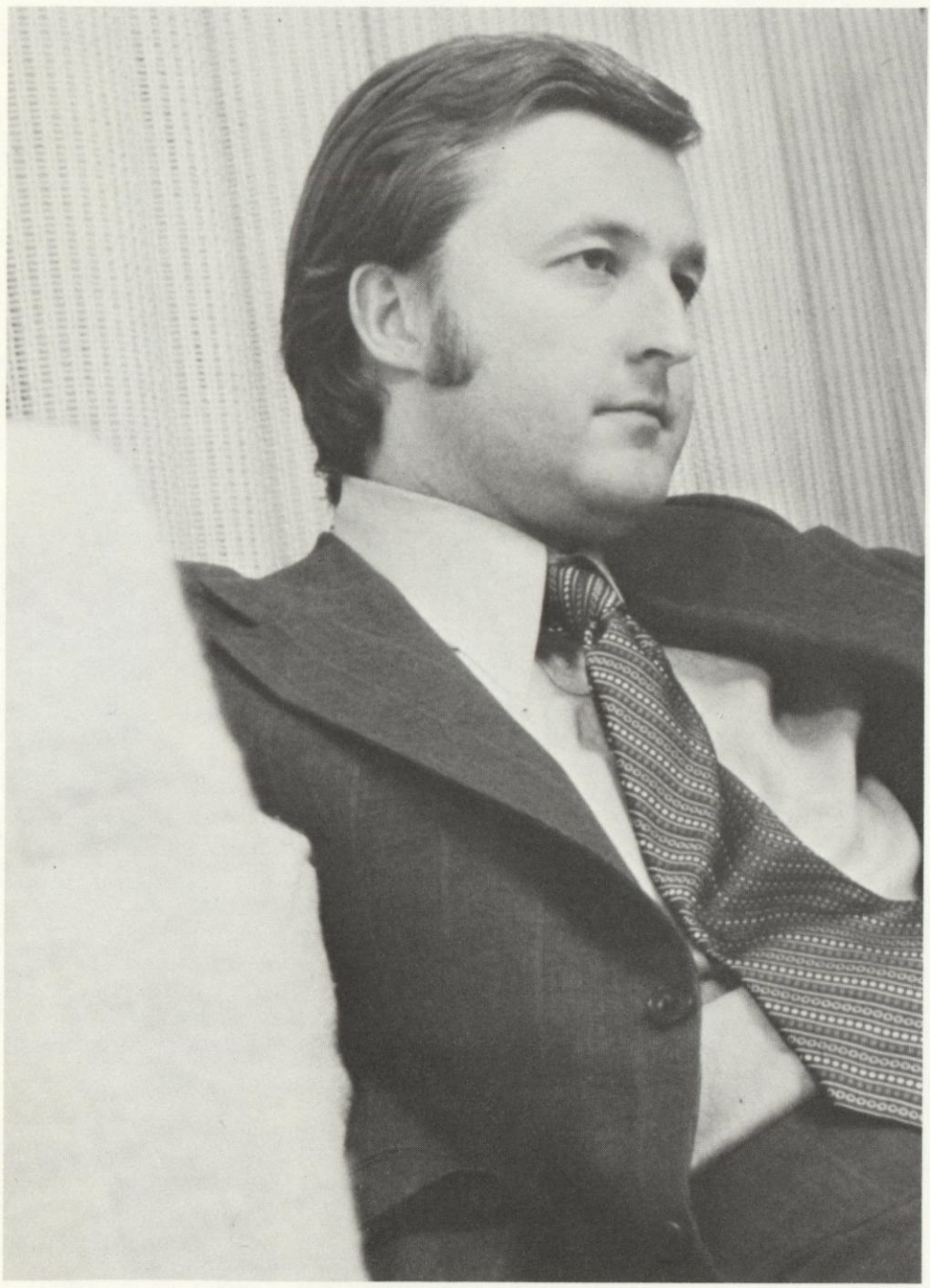
President's Letter



To our shareholders:

Fiscal 1973 was a disappointing year for National Tea, a year beset by problems. It was a year in which the Company experienced an operating loss of $9,093,784 and an extraordinary loss of $26,866,473 after taxes.

It is unnecessary for me to elaborate in great detail on the considerable pressures which have been brought to bear on the food retailing industry. We find ourselves embroiled in a classic cost-price squeeze. Operating costs have increased dramatically yet commensurate price increases have been severely restricted by three basic forces—governmental price and margin control, increased consumer resistance to higher prices and competitive attempts to maintain and build sales volume by intensive, unprecedented price cutting.

Maximum efficiency and general corporate fitness are absolutely essential in this trading environment. During the past fiscal year it became apparent that dramatic changes were necessary in your Company's operations. The purpose of this, my first letter to you as President and Chief Executive Officer, is to outline the changes that will be instituted to turn around the operating results of your Company and achieve its profit potential. These fall into four categories—management changes, operational changes, marketing changes, and asset changes.

Management Changes

In March 1973, I was elected President and Chief Executive Officer by your Board of Directors, with full authority and responsibility for management of all corporate affairs.

My first priority is to provide National Tea with a dynamic, new management team that will provide the aggressive leadership necessary to capitalize on the many opportunities available to our Company. This team will be drawn from both inside and outside the Company. To date, management changes at all levels of responsibility have occurred and extensive restructuring

will take place in the near future.

I have been particularly gratified by the number of outstanding young managers in our industry who have recognized the tremendous potential of National Tea and have agreed to join us in shaping the Company's new direction. There is a basic truth in the adage that a Company's employees are its most important resource. In the future, primary importance will be placed on the selection, development, accountability, and motivation of our personnel.

Operational Changes

Immediately upon my appointment as President, a number of in-depth operational analyses were instituted. These studies revealed substantial opportunities to reduce costs and increase National Tea's efficiency.

- A thorough study has been made of every store and its potential contribution to Company profitability. As a result of this analysis 177 outmoded stores are being closed.
- Distribution facilities and costs have been analysed and sizable annual savings identified. A program is being developed to capture these savings as soon as possible.
- An Operations Programming function will be instituted to enable us to utilize our labor more effectively. Labor costs represent 80 percent of controllable store expense. Thus, even a minor improvement in labor utilization can have a major impact on profitability.
- Our analysis indicates that procurement costs and inventory levels can be reduced. The corporate buying function has been completely restructured and a detailed, ongoing program is being developed to reduce inventory investment.

Marketing Changes

At the same time as costs are being reduced, sales must be increased. Decreasing gross margins and rising expenses necessitate increased sales volume to cover fixed overheads and provide an adequate return on investment. A number of changes will be made to provide National Tea with additional marketing thrust.

- A completely new interior and exterior store decor program is being developed that will provide National Tea's customers with a greatly improved shopping environment.
- A new National Tea corporate identity program will be implemented.
- A thorough analysis of individual store potential indicated that substantial sale increases could be achieved through the extension and renovation of selected units. Many of these units will be refurnished during the coming year to incorporate both revised merchandising concepts and our new corporate image package.
- In addition, we will open a number of new stores in excess of 25,000 square feet to maximize operating efficiencies and allow for a more profitable product mix.
- Finally and perhaps most important, the merchandising skills of our organization have already been supplemented by the addition of key personnel who have demonstrated an ability to develop high sales volume units and operate them profitably.

Asset Changes

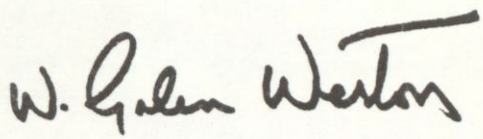
During the past year an extraordinary loss of $26,866,473 was incurred by the disposal of sold operations and the costs resulting from a major store closing program. Of particular consequence was the loss incurred in the disposal of the Pittsburgh/Youngstown Division which arose largely as a result of delays occasioned by labor unions obtaining injunctions that were eventually discharged.

The decision to incur these extraordinary expenses at this time represents your new management's determination to restructure National Tea's assets. The purpose of this restructuring is to identify those operating assets with greatest profit potential as well as provide a meaningful background against which future performance can be measured. The phasing out of these unprofitable elements of the Company will be of material assistance in restoring National Tea's profitability. After phasing out unprofitable units, the net worth of National Tea is more than $92 million, or about $11.84 a share.

During the past year your Company's holdings in Loblaw Inc. were sold for $26,042,122. This transaction provides us with the vital capital necessary to fund the development of new units and the renovation of existing units in critical areas such as the greater Chicago marketplace where the bulk of our assets are located.

Summary

Fiscal 1973 was a year beset by severe challenges—a year of transition—a year of change. The loss reported is a disappointment to me, as I know it is to you. The formation of the new management team and the changes I have outlined are directed towards correcting this loss as quickly as possible. I feel confident that the most difficult of National Tea's problems are behind us.



W. Galen Weston
President and Chief
Executive Officer
May 18, 1973

Consolidated Balance Sheet

Assets	March 31, 1973	April 1, 1972 (restated)
Current Assets:		
Cash	$ 5,866,514	$ 6,533,817
Receivables—		
Trade	8,490,039	13,700,460
Due from sale of Loblaw Inc.	26,042,122	—
Income taxes recoverable from loss carrybacks	8,150,740	—
Inventories	89,989,542	98,893,956
Prepaid expenses, etc.	4,472,806	5,300,892
Real estate in process of development and sale	623,691	754,543
Total current assets	$143,635,454	$125,183,668
Other Assets:		
Investment in net assets of Loblaw Inc.	$ —	$ 26,757,470
Long-term receivables, miscellaneous investments, etc.	5,742,059	4,835,128
	$ 5,742,059	$ 31,592,598
Property and Equipment, at cost:		
Land	$ 2,011,628	$ 2,288,968
Buildings	6,875,877	7,206,901
Fixtures and equipment	124,019,658	139,371,491
Reserves for depreciation (including reserve of $5,477,000 in 1973 for loss on disposition of fixtures and equipment)	(72,373,688)	(76,564,385)
Leasehold improvements, less amortization and reserve of $1,057,000 in 1973 for loss on disposition of leaseholds	18,294,457	21,893,829
	$ 78,827,932	$ 94,196,804
Cost of subsidiaries at dates of acquisition in excess of book value	825,411	825,411
	$ 79,653,343	$ 95,022,215
	$229,030,856	**$251,798,481**

The accompanying notes are an integral part of this statement.

National Tea Co. & Subsidiaries

Liabilities	March 31, 1973	April 1, 1972 (restated)
Current Liabilities:		
Bank loans	$ 4,000,000	$ —
Current maturities of long-term debt	5,223,166	2,456,868
Accounts payable	50,460,418	47,403,139
Accrued liabilities	15,798,539	8,271,941
Income taxes	1,071,559	2,597,223
Total current liabilities	$ 76,553,682	$ 60,729,171
Long-Term Debt:		
Revolving credit notes (convertible into a bank term loan)	$ 37,830,000	$ 39,000,000
5% sinking fund debentures, due 1977	4,680,000	5,280,000
4% promissory notes	—	2,800,000
Equipment purchase obligations, due from 1974 to 1978	3,391,931	1,669,852
Installment mortgage notes, maturing from 1974 to 1983	402,143	463,229
3½% subordinated debentures, due 1980	2,313,000	2,313,000
	$ 48,617,074	$ 51,526,081
Other Liabilities:	$ 10,951,777	$ 7,641,172
Shareholders' Investment:		
Common shares, $4 par value, authorized 10,000,000 shares; issued 8,756,788 shares	$ 35,027,152	$ 35,027,152
Paid-in capital (no transactions during year)	30,823,955	30,823,955
Retained earnings	42,033,584	81,027,318
	$107,884,691	$146,878,425
Less cost of 910,132 common shares in treasury	(14,976,368)	(14,976,368)
	$ 92,908,323	$131,902,057
	$229,030,856	**$251,798,481**

Statements of Consolidated Income and Retained Earnings

	Fifty-Two Weeks Ended March 31, 1973	Fifty-Two Weeks Ended April 1, 1972 (restated)
Income:		
Sales	$1,089,752,837	$1,088,267,596
Costs and Expenses:		
Cost of sales, occupancy, buying and other operating expenses	$ 927,072,294	$ 919,557,742
Selling, general and administrative expenses	171,251,436	152,939,617
Interest expense, net	2,704,505	2,624,211
Profit sharing	—	285,000
Taxes on income—		
Payable (refundable) currently	(3,340,000)	4,682,000
Deferred	(2,161,000)	196,000
	$1,095,527,235	$1,080,284,570
Income (loss) from continuing operations	$ (5,774,398)	$ 7,983,026
Income (Loss) From Sold and Discontinued Operations, net of related income tax benefits of $3,698,000 in 1973 and taxes of $821,000 in 1972	(3,319,386)	937,227
Income (loss) before extraordinary items	$ (9,093,784)	$ 8,920,253
Extraordinary Items, net of related tax benefits of $2,980,000	(26,866,473)	—
Net income (loss)	**$ (35,960,257)**	**$ 8,920,253**
Income (Loss) per Common Share:		
Continuing operations	$(.76)	$1.05
Sold and discontinued operations	(.44)	.13
Before extraordinary items	$(1.20)	$1.18
Extraordinary items	(3.54)	—
Net income (loss)	$(4.74)	$1.18
Retained Earnings:		
Balance—Beginning of period	$ 81,027,318	$ 78,174,019
Add (Deduct) –		
Net income (loss)	(35,960,257)	8,920,253
Dividends ($.40 in 1973 and $.80 in 1972 per share)	(3,033,477)	(6,066,954)
Balance—End of period	**$ 42,033,584**	**$ 81,027,318**

The accompanying notes are an integral part of these statements.

Statement of Consolidated Changes in Financial Position

	Fifty-Two Weeks Ended March 31, 1973	Fifty-Two Weeks Ended April 1, 1972 (Restated)
Working capital provided by:		
Income (loss) before extraordinary items	$ (9,093,784)	$ 8,920,253
Non-cash items not requiring working capital—		
Depreciation and amortization	13,586,759	14,393,216
Deferred taxes	(3,210,000)	196,000
Other	1,138,569	(2,503,475)
Working capital provided by operations	$ 2,421,544	$21,005,994
Extraordinary items (portion requiring the use of working capital)	(10,716,431)	—
Dispositions of property and equipment	5,309,504	3,054,237
Proceeds from bank term loan refinanced	—	11,500,000
Proceeds from equipment purchase obligations	3,066,776	3,011,093
Sale of Loblaw Inc.	26,042,122	—
Other, net	1,267,004	(806,430)
Total working capital provided	$ 27,390,519	$37,764,894
Working capital used for:		
Cash dividends to shareholders	$ 3,033,477	$ 6,066,954
Additions to property and equipment	15,753,984	19,527,429
Maturities of long-term debt	5,975,783	2,883,736
Total working capital used	$ 24,763,244	$28,478,119
Increase in working capital	$ 2,627,275	$ 9,286,775
Increase in working capital represented by:		
Increase (decrease) in current assets—		
Cash	$ (667,303)	$ (3,509,094)
Receivables	28,982,441	3,836,997
Inventories	(8,904,414)	(2,107,424)
Prepaid expenses, etc.	(828,086)	1,547,207
Real estate in process of development and sale	(130,852)	90,645
	$ 18,451,786	$ (141,669)
(Increase) decrease in current liabilities—		
Bank loans	$ (4,000,000)	$ —
Current maturities of long-term debt	(2,766,298)	1,640,132
Accounts payable	(3,057,279)	6,873,126
Accrued liabilities	(7,526,598)	104,488
Income taxes	1,525,664	810,698
	$(15,824,511)	$ 9,428,444
Increase in working capital	**$ 2,627,275**	**$ 9,286,775**

The accompanying notes are an integral part of this statement.

Notes to Consolidated Financial Statements

March 31, 1973

1. Summary of Significant Accounting Policies

The following are the significant accounting policies of the company and its subsidiaries:

Principles of consolidation—The consolidated financial statements include the accounts of the company and its wholly owned subsidiaries except Loblaw Inc. and its subsidiaries which are included on the basis of the company's equity in the net assets of these companies because they were sold subsequent to year end. All significant inter-company transactions have been eliminated in the accompanying consolidated financial statements.

Inventories—Retail store grocery inventories are stated at the lower of cost or market using the retail method. All other inventories are stated at the lower of average cost or market.

Property and equipment—For financial reporting purposes, fixtures and equipment are depreciated by the companies using the straight line composite method, at rates which will amortize the cost of these assets over their estimated useful lives; buildings are depreciated at straight-line rates over their estimated useful lives; leasehold improvements are amortized at straight-line rates over their estimated useful lives or the term of the lease, whichever is less. For tax purposes, accelerated methods are used for fixtures and equipment. Any gain or loss from the sale or other disposal of land and buildings is included in income. No gain or loss is recognized on normal dispositions of fixtures and equipment; the gross asset value is removed from the accounts and any proceeds are credited to the reserve for depreciation. Any gain or loss on major dispositions of fixtures and equipment is included in income.

Cost of subsidiaries at dates of acquisition in excess of book value—The cost of subsidiaries at dates of acquisition in excess of book value relates to businesses acquired in transactions initiated prior to November 1, 1970, and is not being amortized by the company.

Taxes on Income—Taxes on income are provided by the companies based on income reported for financial statement purposes. Deferred income taxes arise principally from the use of accelerated depreciation for income tax purposes. Investment tax credits are reflected as a reduction (flow-through method) of taxes on income payable currently.

Store opening costs—Expenditures of a noncapital nature incurred prior to the opening of a new store are charged to expense as incurred.

Earnings per share—Earnings per common share have been computed based upon the weighted average number of shares outstanding. 262,963 shares of National Tea Co. stock held by Loblaw Inc. have been treated as treasury stock for purposes of computing earnings per share.

2. Sale of Loblaw Inc.

As of March 31, 1973, the company sold for approximately $26,000,000 its investment (73% of the outstanding common stock) in Loblaw Inc. to Loblaw Groceterias Co., Limited which owns 55% of the outstanding common shares of the company. The price was equivalent to the net book value of the company's investment in Loblaw Inc.

Loblaw Inc. is a food chain headquartered in Buffalo, New York, which had sales of $329,662,000 and $329,688,000 in fiscal years 1973 and 1972 respectively. The company's share of Loblaw Inc.'s net loss for 1973 was $128,000 and net income for 1972 was $2,343,000.

The consolidated financial statements as of April 1, 1972, have been restated so as to exclude the accounts of Loblaw Inc. As a result of the sale, the treasury shares of National decreased by the 262,963 shares owned by Loblaw Inc. The company's equity in the earnings of Loblaw Inc. is included in the accompanying statement of consolidated income in the caption "Income (Loss) from Sold and Discontinued Operations". The company's equity in the net assets is included in receivables at March 31, 1973, and will be paid in cash upon completion of the contract.

3. Long-Term Debt

Under the terms of an agreement securing the revolving credit notes, the company may convert any or all of the revolving credit notes outstanding on July 1, 1973 to a bank term loan in an amount not to exceed $39,000,000. Repayments are required from 1974 to 1979. Annual amounts due are included in the maturities of long-term debt shown below. Interest rates on the revolving credit notes and the term loan vary with the prime rate, being ¼% and ½% over prime, respectively. The interest rate on the notes at May 18, 1973 was 7¼%.

Aggregate maturities and sinking fund requirements under long-term loan agreements, exclusive of minor installments due on store building mortgage loans and assuming conversion of the $39,000,000 of revolving credit notes to a term loan, are $5,223,000 in 1974, $4,958,000 in 1975, $6,908,000 in 1976, $8,468,000 in 1977, and $11,918,000 in 1978.

The revolving credit and term loan agreement contains certain restrictions which, among other things, restrict the company's payment of cash dividends and acquisition of its capital stock to earnings subsequent to April 3, 1971 (the note holders waived the restriction for the second quarter 1973 dividend); accordingly, the company may not pay dividends or reacquire its capital stock until retained earnings exceed $78,174,019. In addition, the company is required to maintain consolidated working capital of not less than $65,000,000; this requirement increases $5,000,000 on March 30, 1975.

4. Extraordinary Items

During 1973, the company sold 52 stores in the Pittsburgh/Youngstown division at approximately book value. The remaining 32 stores and the warehouse of that division together with 62 unprofitable stores in other divisions were closed. The company intends to close additional stores after year end. Provision for losses on disposition of fixtures, equipment and leasehold improvements, and lease obligations, losses on inventory liquidations; severance pay, etc. were recorded as extraordinary items and consist of the following:

Rent paid and provision for loss on lease obligations of closed stores, net of estimated sub-lease income	$11,517,910
Provision for losses on fixtures and equipment of closed stores and warehouse facilities	13,429,473
Inventory liquidation losses, severance pay, etc.	4,129,090
Other	770,000
	$29,846,473
Income tax benefits	2,980,000
Total	$26,866,473

5. Income (Loss) from Sold and Discontinued Operations

Income (loss) from sold and discontinued operations includes the company's equity in the earnings of Loblaw Inc. and Subsidiaries, the loss of the Pittsburgh/Youngstown Division prior to management's decision to dispose of the operation and the operations of the stores closed during the year. Sales of these various entities were $435,009,000 in 1973 and $525,585,000 in 1972.

6. Taxes on Income

Tax credits applicable to the company's operating loss and extraordinary charge are based on amounts refundable from loss carryback claims and appropriate adjustments of the deferred income tax account. At March 31, 1973, the company had approximately $25,000,000 of net operating losses which can be offset against future taxable income. $8,700,000 of the loss carryforwards expires in 1978; the balance has not yet been claimed for Federal tax purposes. Upon utilization of these loss carryforwards, $3,500,000 will be restored to deferred income tax reserves. The company also had $497,000 of unused investment tax credits earned in 1973 available until 1978 to offset future taxes payable.

Taxes on income in 1972 are lower in relation to pre-tax income than is customary due primarily to investment tax credits of approximately $950,000 and certain non-taxable income.

7. Lease Commitments

At March 31, 1973, the company and its consolidated subsidiaries had 484 leases (some of which contain percentage rental clauses) expiring more than three years after that date with minimum annual rentals amounting to approximately $17,537,000 exclusive of taxes, insurance and maintenance payable by the lessee. Of this amount, approximately 58% applies to leases expiring within 10 years.

8. Other Liabilities:

Other liabilities include:

	March 31, 1973	April 1, 1972
Reserve for future lease obligations on closed stores, net of estimated sub-lease income	$6,513,164	$ —
Capitalized lease obligation	1,940,000	2,070,000
Deferred income taxes	558,000	4,771,172
Reserve for self-insurance	800,000	800,000
Reserve for deferred compensation	1,140,613	—
	$10,951,777	$7,641,172

Auditors' Report

To The Shareholders of National Tea Co.:

We have examined the consolidated balance sheet of NATIONAL TEA CO. (an Illinois corporation 55% owned by Loblaw Groceterias Co., Limited) AND SUBSIDIARIES as of April 1, 1972, and March 31, 1973, and the related statements of income, retained earnings and changes in financial position for the fiscal years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine the consolidated financial statements of Loblaw Inc. and Subsidiaries, the investment in which is reflected in the accompanying financial statements using the equity method of accounting. These statements were examined by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for Loblaw Inc. and Subsidiaries, is based solely upon the report of the other auditors.

In our opinion, based upon our examination and the report of other auditors referred to above, the accompanying consolidated financial statements referred to above present fairly the financial position of National Tea Co. and Subsidiaries as of April 1, 1972, and March 31, 1973, and the results of their operations and changes in their financial position for the fiscal years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

Arthur Andersen & Co.

Chicago, Illinois,
May 18, 1973.

National Tea Co.

Executive Offices
8303 West Higgins Rd.
Chicago, Illinois 60631

Divisional Offices and Warehouses

Chicago, Minneapolis,
Milwaukee, Indianapolis,
St. Louis, New Orleans, Davenport,
Denver

Transfer Agents

The First National Bank of Chicago
Chicago, Illinois

The Chase Manhattan Bank
New York, New York

Registrars

Continental Illinois National Bank
& Trust Company of Chicago
Chicago, Illinois

Chemical Bank
New York, New York

Transfer and Paying Agents

3½% Debentures
Chemical Bank
New York, New York

5% Debentures
Morgan Guaranty Trust Company
New York, New York

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